

Date Mailed October 15, 2001
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BEFORE THE  
PUBLIC SERVICE COMMISSION OF WISCONSIN

In the Matter of Rulemaking to Revise Wis. Admin. Code Chapter  
PSC 163, Telecommunications Utility Price Regulation, Regarding  
the Productivity Offset Factor

1-AC-193

Clearinghouse No. 00-155

**PROPOSED ORDER ADOPTING RULES**

The Public Service Commission of Wisconsin proposes an order to amend PSC  
163.04(2)(b) and create PSC 163.04(2)(br) relating to the telecommunications utilities price  
regulation productivity factor.

**REPORT TO THE LEGISLATURE**

Set forth herein as Attachment A.

**FISCAL ESTIMATE**

This rule change has no fiscal impact. A completed Fiscal Estimate form is included as  
Attachment B.

**EFFECTIVE DATE**

These rules shall take effect on the first day of the month following publication in the  
Wisconsin administrative register as provided in s. 227.22(2)(intro.), Stats.

### **CONTACT PERSON**

Questions from the media may be directed to Jeffrey L. Butson, Public Affairs Director at (608) 267-0912. Other questions regarding this matter should be directed to Christopher Larson, docket coordinator, at (608) 267-9508, or by email at *larsoc@psc.state.wi.us*. Hearing or speech-impaired individuals may also use the Commission's TTY number, (608) 267-1479.

The Commission does not discriminate on the basis of disability in the provision of programs, services, or employment. Any person with a disability who needs accommodations to participate in this proceeding or who needs to obtain this document in a different format should contact the docket coordinator listed above.

Dated at Madison, Wisconsin, \_\_\_\_\_

By the Commission:

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Lynda L. Dorr  
Secretary to the Commission

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Attachments

## **REPORT TO THE LEGISLATURE**

### **A. NEED FOR THE RULE**

Section 196.196(1)(c), Stats., provides for the use of a productivity offset mechanism in determining the amount a price-regulated company may increase or shall decrease its rates for price-regulated services. Pursuant to this section, the first time the productivity offset may be changed is after September 1, 2000. Section PSC 163.04(2)(b) sets forth the factors the Commission may consider in determining any statewide changes in productivity. Under this rule, the Commission shall provide for a productivity study for the telecommunications industry in the state.

In docket 05-TI-174, Investigation of Telecommunications Utility Price Regulation Pursuant to §196.196(1)(g), Stats., the Commission found that a rulemaking proceeding should be initiated at this time to review the productivity offset.

### **B. PLAIN LANGUAGE ANALYSIS**

Statutory Authority: ss. 196.02(3), 196.196(1)(c), and 227.11, Stats.  
Statutes Interpreted: s. 196.196(1)(c)1., Stats.

The objective of the proposed rule revision in this proceeding is to make those changes to s. PSC 163.04(2)(b) regarding the productivity offset factor deemed necessary as a result of a productivity study for the telecommunications industry in the state pursuant to s. PSC 163.04(2)(bm). Pursuant to s. PSC 163.04(2)(bm), each time the productivity factors are reviewed, the Commission shall provide for a productivity study for the telecommunications industry in this state. This study shall address the factors set forth in s. PSC 163.04(2)(b) plus additional evidence relative to a utility's ability to increase productivity in the future.

The proposed rule revisions interpret s. 196.196(1)(c)1., Stats., to mean that the Commission may, at this time, change the productivity offset by a maximum of one percent, effective immediately and for each of the next two years. The earliest the Commission could examine these factors again would then be three years after the effective date of this rule.

The productivity offset is currently either 2 percent or 3 percent, depending on the number of access lines a utility has when it elects price regulation. The rule revision increases the productivity offset to 3 percent or 4 percent on the effective date of the rule, to 4 percent or 4.3 percent one year later, and to 4.3 percent for all price regulated utilities one year after that.

## C. TEXT OF FINAL RULE

SECTION 1. PSC 163.04(2)(b)(intro.) is amended to read:

**PSC 163.04(2)(b)** ~~According to s. 196.196(1)(e), Stats., the productivity factor offset to the  $\Delta$  GDPPI shall be 2 percentage points. For a telecommunications utility with more than 500,000 access lines, the percentage offset shall be 3 percentage points. Section 196.196(1)(c)1., Stats., sets the GDPPI percentage offset, but provides that Beginning beginning in the year 2000 and every 3 years thereafter, for the purpose of adjusting the GDPPI percentage offset, pursuant to s. 196.196(1)(e), Stats., to reflect any statewide changes in the productivity experience of the telecommunications industry, the commission may consider the following historical factors:~~

SECTION 2. A note following PSC 163.04(2)(b) is created to read:

**Note:** The percentage offsets were originally set at 3 percentage points for utilities with more than 500,000 access lines at the time of electing price regulation, and 2 percentage points for utilities with 500,000 or less access lines at the time of electing price regulation.

SECTION 3. PSC 163.04(2)(br) is created to read:

**PSC 163.04(2)(br)** Based on the most recent statewide productivity study, the productivity factor offset to the  $\Delta$  GDPPI shall be:

1. For telecommunications utilities with 500,000 or less access lines at the time of electing to be price regulated:

a. 3 percentage points, effective on the effective date of this paragraph....[revisor inserts date].

b. 4 percentage points, effective one year after the effective date of this paragraph....[revisor inserts date].

c. 4.3 percentage points, effective two years after the effective date of this paragraph....[revisor inserts date].

2. For telecommunications utilities with more than 500,000 access lines at the time of electing to be price regulated:

a. 4 percentage points, effective on the effective date of this paragraph....[revisor inserts date].

b. 4.3 percentage points, effective one year after the effective date of this paragraph [revisor inserts date].

These rules shall take effect on the first day of the month following publication in the Wisconsin administrative register as provided in s. 227.22 (2) (intro.), Stats.

D. PUBLIC HEARING ATTENDEES

The following are the names of those who attended the public hearings and who submitted written comments concerning the proposed rule.

AMERITECH WISCONSIN

by

Mr. Michael Paulson  
722 North Broadway  
Milwaukee, WI 53202-4396

VERIZON NORTH INC.

by

Stacy Rodriguez  
Carl Lian  
Daniel Matson  
Paul Verhoeven  
P.O. Box 49  
100 Communications Drive  
Sun Prairie, WI 53590-0049

No modifications to the proposed rules were made as a result of the comments submitted in this proceeding. Comments of the parties are summarized in Attachment A1, together with the response from the Commission.

E. RESPONSE TO LEGISLATIVE COUNCIL REPORT

A copy of the Legislative Council's report, and responses to it, are included with this Report as Attachment A2.

F. FINAL REGULATORY FLEXIBILITY ANALYSIS

These rules may have an effect on small telecommunications utilities, which are small businesses under s. 196.216, Stats., for the purposes of s. 227.114, Stats., because they may elect to become price-regulated under s. 196.196(1), Stats., which would result in these rules becoming applicable to them. The agency has considered the methods in s. 227.114(2), Stats., for reducing the impact of the rules on small telecommunications utilities and finds that incorporating any of these methods into the proposed rules would be contrary to the statutory objectives which are the basis for the proposed rules. In addition, the election of price regulation under this chapter is voluntary, and more flexibility and less stringent compliance requirements for small telecommunications utilities are available in ss. 196.195 (12) and 196.196 (4), Stats.

There are 84 local exchange companies in Wisconsin, 77 of which are small telecommunications utilities. The agency finds that the availability of a voluntary price regulation

election under s. 196.196, Stats., and the process set forth in this chapter to govern the price regulation election are in the public interest for all telecommunications utilities in the state.

## Comments and Responses

### **Verizon North Inc.**

#### **Comment:**

The proposed rule revisions are contrary to s. 196.196(1)(c)1., Stats., in that they assume that the productivity offset can be changed by 1 percent each year during the 3-year period between productivity studies. Productivity offset cannot change by more than 1 percent in any review period.

#### **Response:**

Construing the statute as Verizon suggests makes the statutory language “in any 12-month period” meaningless. The plain language of the statute allows the commission to act to adjust the productivity offset factor percentage every 3 years and to adjust it by 1 percent in each of the 3 years.

#### **Comment:**

The staff productivity study is fatally flawed because it violates the fundamental principles of price regulation and is inconsistent with sound economic theory. Rather than examine the productivity of the telecommunications industry as a whole, it examines company-specific cost and revenue data. For example, the staff study includes an adjustment for the estimated merger cost savings resulting from the GTE/ Bell Atlantic and Ameritech/SBC mergers.

#### **Response:**

Staff’s study combines company-specific data from all local exchange companies in the state into a statewide examination of telecommunications industry productivity. This is required by s. PSC 163.04(2)(bm).

Verizon argues that it is inappropriate to consider company-specific merger savings in the productivity study. The code, however, allows such savings to be considered:

...this study...shall address the above factors plus additional evidence relative to a utility’s ability to increase productivity in the future. [s. PSC 163.04(2)(bm)].

Verizon argues that consideration of merger savings would violate a fundamental principle of price regulation by penalizing efficient companies. It claims that the fundamental principle of price regulation is to sever the link between a regulated company’s cost and prices. Contrary to Verizon’s assertion, use of the staff study would not recapture all of the merger savings by any means. The productivity factor established in this proceeding will apply to only

price regulated services, which account for less than 20 percent of Ameritech's total operating revenues, and less than 30 percent for Verizon. Ameritech and Verizon are therefore able to retain 70 to 80 percent of their productivity gains as additional net income.

In addition, Ameritech and Verizon would retain the excess of their productivity gains over the statewide average. Staff's study uses an average statewide productivity estimate, so that estimated merger savings are averaged in with the other incumbent local exchange companies in the state. There is no doubt that merger-related productivity gains are a part of the overall productivity changes experienced by the telecommunications industry in this state.

**Comment:**

The staff study is incomplete and unsupported. The staff study excludes several items normally included in net investment rate base because the data was not readily available or such data would have made an immaterial difference.

**Response:**

Excluding items because the data was not readily available, or because inclusion would have made an immaterial difference, are routine problems that are encountered in any similar study. In this case, staff excluded data related to plant under construction and deferred income taxes. In any study, one needs to use the best information available at the time of the study. Since certain information was not available for all companies or reported information was not consistent from year-to-year, staff determined that the data related to plant under construction and deferred income taxes was flawed and any study based on such data would be flawed. Regarding the materiality question, staff excluded data related to materials and supplies and RTB Class B Stock. Such data was considered by staff to be immaterial to this productivity study. To be efficient in the completion of any study, there needs to be materiality limits. Without materiality limits, time would be wasted reflecting factors that would have no impact on the results of the study.

**Comment:**

Verizon North's study reflects price regulation theory. Verizon conducted several separate productivity studies based on well-accepted economic principles. Based on Verizon's studies, the productivity offset factor should be 0.77 percent. However, due to statutory limitations, the productivity offset factor should be reduced to 1 percent or, at least maintained at the current 2 percent.

**Response:**

While the applicable statutes and rules allow a good deal of flexibility in determining an appropriate productivity factor, the requirement to examine statewide data is clear:

...the commission may...(change the productivity offset)... to reflect any statewide changes in the productivity experience of the telecommunications industry.[s. 196.196(1)(c)1., Stats.]



Each time the productivity factors are reviewed, the commission shall provide for a productivity study for the telecommunications industry in this state. [s. PSC 163.04 (2)(bm)]

Regardless of any arguments about the theoretical validity of different methodologies, the Commission's use of Verizon's study would be unlawful, because it uses national measures of productivity rather than statewide measures.

The Commission discussed hiring an outside firm to conduct a study. Due to budgetary and time constraints, Ameritech and Verizon were asked to agree to be directly billed by a Commission-approved consultant. (The statute provides for price-regulated companies to pay for this study.) Both companies declined. As a result, staff performed its own study using the best available information.

### **Ameritech Wisconsin**

#### **Comment:**

Has not done an independent total factor productivity study for statewide telecommunications industry in Wisconsin, so did not comment on the results of the study.

#### **Comment:**

Recommends that Commission reject the proposed rule to the extent that it increases the productivity offset by more than 1 percent over the next three years. Believes that the legal conclusion embodied in the proposed rule contradicts s. 196.196(1)(c)1., Stats., by attempting to adjust the productivity offset three times over the next three years.

#### **Response:**

Construing the statute as Ameritech suggests makes the statutory language "in any 12-month period" meaningless. The plain language of the statute allows the commission to act to adjust the productivity offset factor percentage every 3 years and to adjust it by 1 percent in each of the 3 years.

**Response to Report from Legislative Council**

**2. Form, Style and Placement in Administrative Code**

- a. Agree. Suggested change done.
- b. Agree. Suggested changes done.
- c. Agree. Suggested change done.
- d. Agree. Suggested change done.
- e. Agree. Suggested change done.
- f. Agree. Suggested change done.

**4. Adequacy of References to Related Statutes, Rules and Forms**

- a. Agree. Suggested change done.
- b. Agree. Suggested change done.

<b>2001 Session</b>	
<b>FISCAL ESTIMATE</b> DOA-2048 N(R10/96)	<div style="display: flex; justify-content: space-between;"> <span>X ORIGINAL</span> <span><input type="checkbox"/> UPDATED</span> </div> <div style="display: flex; justify-content: space-between;"> <span><input type="checkbox"/> CORRECTED</span> <span><input type="checkbox"/> SUPPLEMENTAL</span> </div>
<div style="border: 1px solid black; padding: 2px; margin-bottom: 2px;">LRB or Bill No./Adm. Rule No.</div> <div style="border: 1px solid black; padding: 2px;">Amendment No. if Applicable</div>	
<b>Subject</b> In the Matter of Proposed Revision for a Rulemaking of Wis. Admin. Code Chapter PSC 163 Telecommunications Utility Price Regulation, Regarding the Productivity Offset Factor	
<b>Fiscal Effect</b> <b>State:</b> X No State Fiscal Effect Check columns below only if bill makes a direct appropriation or affects a sum sufficient appropriation. <div style="display: flex; justify-content: space-between; margin-top: 10px;"> <div style="width: 60%;"> <input type="checkbox"/> Increase Existing Appropriation    <input type="checkbox"/> Increase Existing Revenues  <input type="checkbox"/> Decrease Existing Appropriation    <input type="checkbox"/> Decrease Existing Revenues  <input type="checkbox"/> Create New Appropriation         </div> <div style="width: 35%; border-left: 1px solid black; padding-left: 10px;"> <input type="checkbox"/> Increase Costs - May be possible to Absorb Within Agency's Budget    <input type="checkbox"/> Yes    <input type="checkbox"/> No   <input type="checkbox"/> Decrease Costs         </div> </div>	
<b>Local:</b> X No local government costs <div style="display: flex; justify-content: space-between; margin-top: 10px;"> <div style="width: 30%;">           1. <input type="checkbox"/> Increase Costs                  <input type="checkbox"/> Permissive    <input type="checkbox"/> Mandatory            2. <input type="checkbox"/> Decrease Costs                  <input type="checkbox"/> Permissive    <input type="checkbox"/> Mandatory         </div> <div style="width: 30%;">           3. <input type="checkbox"/> Increase Revenues                  <input type="checkbox"/> Permissive    <input type="checkbox"/> Mandatory            4. <input type="checkbox"/> Decrease Revenues                  <input type="checkbox"/> Permissive    <input type="checkbox"/> Mandatory         </div> <div style="width: 35%; border-left: 1px solid black; padding-left: 10px;">           5. Types of Local Governmental Units Affected:  <input type="checkbox"/> Towns    <input type="checkbox"/> Villages    <input type="checkbox"/> Cities  <input type="checkbox"/> Counties    <input type="checkbox"/> Others _____  <input type="checkbox"/> School Districts    <input type="checkbox"/> WTCS Districts         </div> </div>	
<b>Fund Sources Affected</b> <input type="checkbox"/> GPR <input type="checkbox"/> FED <input type="checkbox"/> PRO <input type="checkbox"/> PRS <input type="checkbox"/> SEG <input type="checkbox"/> SEG-S	<b>Affected Ch. 20 Appropriations</b>
<b>Assumptions Used in Arriving at Fiscal Estimate</b>  <p>Section 196.196(1)(c), Stats., provides for the use of a productivity offset mechanism in determining the amount a price-regulated company may increase or shall decrease its rates for price-regulated services. According to this section, the productivity factor offset to the change in the gross domestic product price index (GDPPI) shall be 2 percentage points. For a telecommunications utility with more than 500,000 access lines, the percentage offset shall be 3 percentage points. Pursuant to s. 196.196(1)(c), Stats., the first time the productivity offset may be changed is after September 1, 2000. Section PSC 163.04(2)(b) sets forth the factors the Commission may consider in determining any statewide changes in productivity.</p> <p>The objective of the proposed rule revision in this proceeding is to make those changes to s. PSC 163.04(2)(b) regarding the productivity offset factor deemed necessary as a result of a productivity study for the telecommunications industry in the state pursuant to s. PSC 163.04(2)(bm). Pursuant to s. PSC 163.04(2)(bm), each time the productivity factors are reviewed, the Commission shall provide for a productivity study for the telecommunications industry in this state.</p> <p>These proposed rule revisions are considered minor in nature and should not require a change in staffing needs or any other changes in costs. Therefore, no fiscal impact is expected.</p>	
<b>Long-Range Fiscal Implications</b>  <b>NONE</b>	
<b>Agency/Prepared by: (Name &amp; Phone No.)</b>  Gordon Grant/608-267-9086	<div style="display: flex; justify-content: space-between;"> <div style="width: 60%;"> <b>Authorized Signature/Telephone No.</b>   </div> <div style="width: 35%;"> <b>Date</b>           January 26, 2001       </div> </div>